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MITI White Paper Stresses Stability, Policy Coordination

The Ministry of International Trade and Industry has prepared 40 White Papers on International Trade over the years. Each one reviews the previous year, highlighting problems and making recommendations. Past documents have alternated between descriptions of serious setbacks such as the two oil shocks of the 1970s and declarations of triumphs like the rapid growth in exports of the 1960s. The 1987 version is a hybrid, covering a period of crises averted and potentially serious problems overcome or postponed. The stock market crashed, protectionist sentiment in the United States and elsewhere continued and the yen soared to new heights. While each carried the potential for disaster, the Japanese economy somehow overcame each.

Japan's Services Deficit Rises

Japan's overall current account surplus is inching downward but one component is changing rapidly. The already large services deficit widened last year, reversing the 1981-86 pattern of declining deficits. The increase occurred despite much higher investment income attributable mostly to the continued recycling of Japan's current account surpluses into capital flows overseas. As in the past this income in 1987 consisted mainly of dividends and interest earned on securities and loans rather than profits from manufacturing plants, distribution operations and other forms of direct investment (Table 1).

Table 1: Japan's Trade Balance in Services

(in millions of dollars)

Year	Investment Income		Other Services	Total
	Total	Direct		
1978	$900	$376	$-8,287	$-7,387
1979	2,011	345	-11,483	-9,472
1980	854	809	-12,197	-11,343
1981	-763	816	-12,810	-13,573
1982	1,718	992	-11,566	-9,848
1983	3,082	1,354	-12,188	-9,106
1984	4,231	1,428	-11,978	-7,747
1985	6,840	1,711	-12,005	-5,165
1986	9,473	1,412	-14,405	-4,932
1987	16,670	2,004	-22,372	-5,702

Source: Bank of Japan

Credit or blame for the turnaround in 1987 belongs in part to the Japanese tourist, whose purchases of airline tickets get counted as part of the transportation account, with expenditures abroad for hotels, meals and gifts coming under the travel account. Passenger fare payments by Japanese jumped 54.2 percent and travel expenditures soared 48.9 percent in 1987, resulting in the large deficits in both transportation and travel shown in Table 2.

Table 2: Detail of Japan's Services Trade, 1987

(in millions of dollars)

	Credits (Exports)	Debits (Imports)	Net Balance
Transportation	$12,954	$19,060	$-6,106
Travel	2,097	10,760	-8,663
Investment Income	49,245	32,575	16,670
Other Private Transactions	12,617	22,506	-9,889
Official Transactions	2,727	441	2,286
Total	79,640	85,342	-5,702

Source: Bank of Japan

In recent years services trade has attracted increasing attention from American policymakers. Most of their interest is focused on items that Japan includes in "other private transactions." Covered by this category are management fees, patent royalties, agent fees, advertising, film rentals and some insurance receipts and payments. Despite the attention, these transactions account for 26.4 percent of reported imports of services and just 10.5 percent of total Japanese payments for goods and services in 1987.

Of course, the low figure could reflect barriers that prevent trade in services from occurring. For example, if U.S. construction firms win business in Japan as a result of recent market-opening moves and provide design services out of their U.S. offices, it would be recorded in the "other" figure. In addition, there is reason to believe that both exports and imports of services in this category are underreported.

Services are one of the principal items on the agenda for the Uruguay Round of multilateral trade negotiations. Japan has expressed support for the U.S. position of liberalizing services trade within the General Agreement on Tariffs and Trade framework. In late May it submitted a proposal intended to lead to new rules concerning banking, insurance, tourism and information. The proposal would insure other signatories the same opportunities domestic firms have, a principle known as national treatment, and clarify the remaining rules. Liberalizing services trade has gotten a lukewarm reception from many developing countries, which initially resisted even putting this subject on the GATT agenda.

Douglas Ostrom

Science And Technology Agreement May Be Finalized At Toronto Summit

In addition to addressing macroeconomic policy and trade issues at the June 19-21 economic summit in Toronto, the United States and Japan may use this opportunity to formally conclude a revised agreement governing bilateral science and technology cooperation. Japanese Ambassador Nobuo Matsunaga stated recently that Tokyo and Washington have been considering holding a special signing ceremony for the accord during the meetings. Both parties agreed on the substance of the new five-year pact March 31 (see JEI Report No. 14B, April 8, 1988), but felt that an additional three months were needed to iron out minor drafting differences.

U.S. observers hope that this agreement will open the door to a reciprocal flow of science and technology. Washington was the primary mover behind the negotiations to revise the existing 1980 accord, which it regarded as so vague that it had enabled Japan to easily exploit American research and development work in leading-edge technologies and improve its competitive position in certain fields at the expense of American industry. Thus, the Reagan administration insisted on more specific guidelines governing bilateral science and technology cooperation. These include:

- the creation of a senior-level government group to discuss science and technology issues;

- the admission of U.S. researchers to projects jointly funded by the private sector and the government;

urged his colleagues to enact a new bill. But others are less sanguine. Finance Committee chairman Lloyd Bentsen (D, Tex.), for example, has estimated the chances for a new trade law this year as no better than 50-50.

It is clearly premature to state that the trade bill has been abandoned. Work on the legislation has continued for roughly three years. Tired of focusing on trade, lawmakers themselves have admitted that they have little incentive to recommence the entire process during the 101th Congress -- little incentive, that is, except for the presidential and congressional elections this November. Not everyone on Capitol Hill believes that holding up passage of a compromise bill because of the plant-closing provision will make good politics. But there are some who do. And on the Senate floor it could take only one amendment to stall the revised bill in its tracks.

Eileen M. Doherty

Notes

Kansai Bidders - On June 6 Kansai International Airport Co., Ltd. announced that 15 of 48 applicants would be allowed to submit detailed bids to design the terminal facilities for the new airport. Eleven of the 15 survivors are foreign. Four are American-Japanese joint ventures -- I.M. Pei & Partners with Kumagai Gumi Co., Ltd.; Ellerbe Beckett/Parsons/Shimizu Partners; Kassabaum Inc. and Kajima Corp./Hellmuth/Obata; and Cesar Pelli and Associates with Takenaka Corp. A New York firm -- Bernard Tschumi Associates -- is also still in the running. So are six European groups: Design System & Architekcten Gemeinschaft (Japan/West Germany); Foster Associates/Ohbayashi Corp. (Great Britain/Japan); Naco/Taller de Arquitectura (Netherlands/Spain); Jean Nouvel et Associes-Sarl (France); Renzo Piano Architecte (France); and Prof. Ungers-Airconsult of West Germany.

The 15 will now submit bids to implement the overall terminal design done by Aeroports de Paris; KIAC expects to pick a final winner by early December. The results of the initial competition are a good start for the recently signed U.S.-Japan accord opening the Japanese public works market to foreign firms (see JEI Report No. 22B, June 10, 1988). The fact that more European applicants survived the first cut than American hopefuls could indicate that an evenhanded approach toward all foreign firms is being taken, allaying European fears of discriminatory treatment.

Primary Dealer Purchases - The Federal Reserve Board gave its consent June 6 to the purchase of primary dealers in U.S. government securities by the Long-Term Credit Bank of Japan, Ltd. and Sanwa Bank, Ltd. Greenwich Capital Markets Inc. will cost the Long-Term Credit Bank $144 million, while the price Sanwa will pay for Brophy, Gestal, Knight & Co. is set at $70 million.

The two applications had been pending for several months, long enough for Japanese bankers to begin to suspect that the Fed was trying to prevent them from establishing a bigger presence in the U.S. Treasury securities market. In its accompanying statement, the Federal Reserve did little to allay this fear, hinting that it would have had no problem accepting a provision in

the omnibus trade bill barring foreign companies from buying primary dealers unless there was reciprocal U.S. access to foreign government debt markets. Since the legislation was vetoed by President Reagan, however, the Fed felt it could delay no longer.

In addition to gaining a coveted primary dealership, LTCB will also get Greenwich Capital Markets' seats on the Chicago Mercantile Exchange and the Chicago Board of Trade. Of the Japanese financial firms active in the U.S. market, only Nikko Securities Co., Ltd. has a seat on the CBOT. Nomura Securities International Inc., Nikko Securities Co. International Inc., Daiwa Securities America Inc. and the Industrial Bank of Japan, Ltd. also own primary government securities dealers, while Fuji Bank, Ltd. recently agreed to acquire a 24.9 percent interest in another of the 42 current dealers.

Agricultural Export Embargoes - The House Foreign Affairs international economic policy and trade subcommittee met June 8 to consider HR 4692, a bill to prohibit embargoes of U.S. agricultural exports except to countries that are engaged ~~in~~ war or military hostilities against the United States. The bill's sponsor, Rep. Bill Alexander (D, Ark.), argued that agricultural sanctions end up harming this country's interests more than those of any other nation. In any case, he said, the United States needs the trade, especially in light of its huge trade deficit. According to the congressman, that U.S. farmers suffer from the sanctions is made all the more frustrating by the fact that agricultural embargoes do not work, especially when U.S. allies do not implement similar sanctions. Mr. Alexander argued that Japan and Western European countries actually benefit from U.S. sanctions on shipments to Cuba and Central America. In fact, however, Japan exports virtually no agricultural products.

The Reagan administration opposes the legislation on the grounds it would limit presidential flexibility in formulating foreign policy. Officials point out that the White House already operates under severe constraints regarding agricultural embargoes. Moreover, Assistant Secretary of State for Economic and Business Affairs Eugene McAllister has indicated that the administration will suggest during the Uruguay Round of multilateral trade negotiations that signatories to the General Agreement on Tariffs and Trade should no longer be permitted to restrict sales of agricultural goods in short-supply situations.

Multilateral Investment Guarantee Agency - Yoshio Terasawa, an executive with Normua Securities Co., Ltd., has been chosen as president of the Multilateral Investment Guarantee Agency. MIGA was established by members of the World Bank and Switzerland to issue guarantees against non-commercial risks to participants that invest in a member developing country (see JEI Report No. 22B, June 12, 1987). Mr. Terasawa's appointment will be formally made June 22 at the first meeting of MIGA. Tokyo, an enthusiastic supporter of the organization, was the first developed country to ratify the convention establishing MIGA.

Japan's FY 1987 Foreign Direct Investment - The multinationalization of Japanese businesses continued at a record-breaking rate in the April 1987-March

1988 period, with companies earmarking $33.4 billion for foreign direct investment on top of a planned expansion of $22.3 billion in FY 1986 and a $12.2 billion projected increase the previous fiscal year. For many firms internationalization has meant establishing a presence in the American market or expanding an existing U.S. operation. That was certainly true in FY 1987. Businesses once again put roughly 45 percent of the money set aside for offshore equity investment into the United States -- a ratio that translated into $14.7 billion compared with $10.2 billion in the 12 months through March 1987. But there were differences in how the rest of the pool of direct investment funds was divvied up geographically. Bigger portions went into Europe ($6.6 billion versus $3.5 billion) and Asia ($4.9 billion, up from $2.3 billion), while investment in Latin America barely topped FY 1986's total at $4.8 billion (see Table 1).

Contrary to the conventional wisdom, financial institutions, not manufacturers, are the leaders of the offshore investment movement. They have accounted for close to one-third of all foreign direct investment in each of the last three fiscal years, channeling $10.7 billion into overseas banking, finance and insurance operations in FY 1987 alone -- nearly 50 percent more than in FY 1986 (see Table 2). The conventional wisdom is not completely off base, however, since Japanese manufacturers more than doubled the amount of money going into offshore production facilities during the April 1987-March 1988 period to $7.8 billion.

While foreign investment in the financial services sector was split fairly evenly among Latin America, Europe and the United States in FY 1986, Europe was the main draw in FY 1987. It attracted $4.5 billion in new capital compared with a $2.9 billion inflow to this country and a $2.6 billion increase in Latin America. For manufacturers, however, the United States remained the prime location. They invested another $4.9 billion here in the year through March 1988 or almost three times more than the $1.7 billion that went into Asia. Similarly, $4.4 billion of the $5.4 billion invested in foreign real estate ventures went into the United States.

The $33.4 billion jump in direct overseas investment in FY 1987 boosted the cumulative total to $139.3 billion (see Table 3). While there is no question that Japanese companies are rapidly expanding their international investment presence, this figure is thought to overstate the size of their equity holdings abroad since it is based on investment plans reported to the Ministry of Finance, not actual flows. A more realistic number, derived from the balance of payments data, was $77.6 billion at the end of 1987 (see JEI Report No. 22B, June 10, 1988).

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The views expressed in this report are those of the authors and do not necessarily represent those of the Japan Economic Institute.

Table 1: Japan's Foreign Direct Investment by Country, FY 1983-FY 1987

(in millions of dollars)

	FY 1983	FY 1984	FY 1985	FY 1986	FY 1987	Cumulative March 31, 1988
United States	$2,565	$3,360	$5,395	$10,165	$14,704	$50,159
Canada	136	184	100	276	653	2,604
North America	2,701	3,544	5,495	10,441	15,357	52,763
Indonesia	374	374	408	250	545	9,218
Hong Kong	563	412	131	502	1,072	4,505
Singapore	322	225	339	302	494	3,065
Korea	129	107	134	436	647	2,765
China	---	114	100	226	1,226	1,740
Malaysia	140	142	79	158	163	1,446
Taiwan	103	65	114	291	367	1,419
Thailand	72	119	48	124	250	1,134
Philippines	65	46	61	21	72	985
Asia	1,847	1,628	1,435	2,327	4,868	26,658
Panama	1,223	1,671	1,533	2,401	2,305	11,146
Brazil	410	318	314	270	229	5,086
Cayman	1	1	132	930	1,197	2,476
Bahama	1	97	298	792	734	1,981
Mexico	121	56	101	226	28	1,584
Peru	---	6	10	---	1	696
Bermuda	14	29	148	16	36	653
Netherlands Antilles	69	66	62	66	199	575
Latin America	1,878	2,290	2,616	4,737	4,816	25,189
United Kingdom	153	318	375	984	2,473	6,598
Luxembourg	265	315	300	1,092	1,764	4,072
Netherlands	113	452	613	651	829	3,166
West Germany	117	245	172	210	403	1,955
France	93	117	67	152	330	1,300
Switzerland	37	229	60	91	224	977
Spain	52	140	91	86	283	883
Belgium	126	71	84	50	70	863
Europe	990	1,937	1,930	3,469	6,576	21,047
Australia	166	105	468	881	1,222	5,724
Oceania	191	157	525	992	1,413	6,647
Liberia	323	281	159	289	267	3,010
Africa	364	326	172	309	272	3,951
Kuwait	66	55	34	41	54	1,363
Iran	1	0	0	---	---	1,003
Middle East	175	273	45	44	62	3,079
Total	8,145	10,155	12,217	22,320	33,364	139,334

Source: Ministry of Finance

Table 2: Japan's Foreign Direct Investment by Sector, FY 1983-FY 1987

(in millions of dollars)

	FY 1983	FY 1984	FY 1985	FY 1986	FY 1987	Cumulative March 31, 1988
Manufacturing Sector	$2,588	$2,505	$2,352	$3,806	$7,832	$36,038
Food Products	77	118	90	127	328	1,546
Textiles	174	85	28	63	206	2,353
Wood and Paper Products	91	115	15	57	317	1,495
Chemicals	450	223	133	355	910	5,247
Metals	479	718	385	328	786	6,304
Nonelectric Machinery	169	185	352	626	687	3,284
Electric Machinery	502	409	513	987	2,421	7,155
Transport Equipment	486	437	627	828	1,473	5,675
Other	160	215	208	435	703	2,980
Nonmanufacturing Sector	5,357	7,429	9,536	17,949	25,080	99,365
Agriculture and Forestry	18	26	12	15	97	893
Fisheries	17	24	42	52	44	538
Mining	382	484	598	669	511	12,936
Construction	55	112	94	250	87	1,134
Trade and Sales	1,164	1,482	1,550	1,861	2,269	16,807
Banking, Finance and Insurance	1,167	2,085	3,805	7,240	10,673	28,772
Services	622	681	665	1,560	2,780	9,026
Transportation	1,363	1,651	1,240	1,925	2,145	9,970
Real Estate	375	430	1,207	3,997	5,428	11,958
Other	193	454	322	379	1,047	7,332
Branch Offices	200	221	329	566	452	3,336
Real Estate Transactions*	---	---	---	---	---	595
Total	8,145	10,155	12,217	22,320	33,364	139,334

*Overseas real estate transactions have been excluded from Japan's foreign direct investment data since December 1, 1980 because of changes in the Foreign Exchange and Foreign Trade Control Law.

Source: Ministry of Finance

Table 3: Japan's Foreign Direct Investment by Industry and Region, March 31, 1988

(in millions of dollars)

	North America	Latin America	Asia	Middle East	Europe	Africa	Oceania	Total
Manufacturing Sector	$14,753	$4,994	$10,000	$1,260	$3,310	$225	$1,496	$36,038
Food Products	724	207	425	0	112	8	68	1,546
Textiles	397	428	1,231	4	245	39	9	2,353
Wood and Paper Products	952	200	212	-	2	0	128	1,495
Chemicals	1,499	562	1,585	1,124	347	19	111	5,247
Metals	1,650	1,764	2,064	59	276	127	364	6,304
Nonelectric Machinery	1,716	361	778	11	365	1	53	3,284
Electric Machinery	4,451	366	1,562	13	704	7	53	7,155
Transport Equipment	2,221	995	1,028	4	797	17	613	5,675
Other	1,142	112	1,115	45	462	7	98	2,980
Nonmanufacturing Sector	36,858	20,126	16,286	448	16,794	3,722	5,131	99,365
Agriculture and Forestry	260	186	262	2	5	7	171	893
Fisheries	139	104	129	1	3	92	69	538
Mining	1,440	1,549	6,677	199	890	579	1,601	12,936
Construction	510	203	254	40	57	21	49	1,134
Trade and Sales	9,727	1,397	1,482	19	3,374	7	801	16,807
Banking, Finance and Insurance	9,149	6,913	1,447	93	10,508	22	640	28,772
Services	3,164	826	3,173	4	540	664	655	9,026
Transportation	188	7,690	393	2	93	1,532	73	9,970
Real Estate	10,130	55	846	-	268	-	658	11,958
Other	2,151	1,203	1,622	87	1,056	798	415	7,332
Branch Offices	667	45	336	1,369	905	1	12	3,336
Real Estate Transactions*	485	23	37	2	38	2	7	595
Total	52,763	25,189	26,658	3,079	21,047	3,951	6,647	139,334

*Overseas real estate transactions have been excluded from Japan's foreign direct investment data since December 1, 1980.

Source: Ministry of Finance